

Office of Chief Counsel
Internal Revenue Service

memorandum

CC:NER:BRK:TL-N-4561-99

TGMcQueeney

date: **OCT 04 1999**

to: Chief, Quality Measurement Branch, Brooklyn District
ATTN: Steven Townsend, Group Manager 1207
R.A. Florence Krein

from: District Counsel, Brooklyn

subject: [REDACTED]
[REDACTED]

DISCLOSURE STATEMENT

This document may include confidential information subject to the attorney-client and deliberative process privileges, and may also have been prepared in anticipation of litigation. This document should not be disclosed to anyone outside the IRS, including the taxpayers involved, and its use within the IRS should be limited to those with a need to review the document in relation to the matter of the case discussed herein. This document is also tax information of the instant taxpayer which is subject to I.R.C. § 6103.

ISSUES

(1) Does the additional information provided by the taxpayer have any impact on the analysis and conclusion in our office's [REDACTED] advisory opinion?

(2) Does the Alternative Minimum Tax at the individual partner level affect the partner's adjusted basis at the partnership level?

CONCLUSION

(1) The additional information provided by the taxpayer does not have any impact on the analysis and conclusion in our office's [REDACTED] advisory opinion.

(2) The Alternative Minimum Tax at the individual partner level does not affect the partner's adjusted basis at the partnership level.

FACTS

On [REDACTED], our office provided a written advisory opinion which was approved by our National Office, copy enclosed, which concluded that the [REDACTED] progress payments received by [REDACTED] road construction partnerships which report income under the completed contract method are unrealized receivables under I.R.C. § 751(c). Our office determined that the progress payments should be treated as advances, where the amounts in excess of adjusted basis are deemed current distributions made on the last day of the partnership taxable year with respect to such partner under Regulation § 1.731-1(a)(i) and (ii) and should be taxed at capital gain rates under Regulation § 1.731-1(a)(3). Since the advances were not a result of a sale or exchange of an interest in a partnership, such amounts in excess of the adjusted basis are not taxed at ordinary income rates until the year of completion or final disposition under I.R.C. § 751. Revenue Rulings 73-301, 79-51 and 82-241 should be followed.

It is our understanding that the taxpayer does not agree with the foregoing analysis and provided additional information to your office. Such information included a [REDACTED] letter to the NYS Department of Transportation and [REDACTED] responses from the NYS Department of Transportation dated [REDACTED] and [REDACTED].

The [REDACTED] letter requested clarification as to under what circumstances the contractor would be under an obligation to repay any payments of estimates. The [REDACTED] response cites [REDACTED], and states that the Department of Transportation's practice and specifications provide for the modification of previously paid estimates and that all project payments may be adjusted or corrected by subsequent estimates or by the final estimate. The [REDACTED] letter stated that the Department of Transportation can and does adjust previous contract payment estimates which may be based upon new engineering calculations, review of actual costs, etc. and may be done in the next payment estimate or in the final estimate. Further, the Department of Transportation is not required to wait for the final payment estimate to make such corrections.

Our office directs your attention to pages [REDACTED] and [REDACTED] of the enclosed [REDACTED] advisory opinion which discusses the information stated in the [REDACTED], [REDACTED], and [REDACTED] letters. Since the information in the three letters was previously considered, such information does not have any impact on the [REDACTED] analysis and conclusion.

It is our understanding that the taxpayer alleges that each partner's adjusted basis in the partnership should be increased due to the Alternative Minimum Tax at the individual partner's level. Specifically, since taxable income from long-term contracts must be determined under the percentage of completion method under I.R.C. § 460(b) for purposes of Alternative Minimum Taxes under I.R.C. § 55, the increase over the taxable income based upon the completed contract method would be reflected on line 14g Long-Term contracts on Form 6251, Alternative Minimum Tax - Individuals. If a partner's adjusted basis is increased, such increase would absorb the taxation of the advances discussed in our [REDACTED] advisory opinion.

ANALYSIS

Subtitle A of the Internal Revenue Code is entitled Income Taxes. Subtitle A is broken down into Chapters and Subchapters. Under Chapter 1 entitled Normal Taxes and Surtaxes, Subchapter A addresses the determination of tax liability and Subchapter K addresses Partners and Partnerships.

I.R.C. §§ 1 and 3 of Subchapter A provide for the regular tax imposed by the tax rate schedules and tax tables for individuals, respectively. In addition to the regular tax imposed, an individual's income tax liability includes any alternative minimum tax (AMT) liability to which the individual is subject under I.R.C. § 55 of Subchapter A.

I.R.C. §§ 701 through 709 of Subchapter K addresses the determination of tax liability for partnerships and partners. Partnerships are not subject to the federal income tax (including the regular tax and the alternative minimum tax). The federal income tax liability arising from income generated by a partnership is borne by the partners in their separate or individual capacities. I.R.C. § 701, Regulations § 1.701-1. Partners, in computing taxable income, take into account separately their distributive shares of the partnership's separately stated items of income, gain, loss, deduction, and credit, and their distributive shares of the partnership's nonseparately stated income or loss. I.R.C. § 702, Regulation § 1.702-1(a). Tax preference items pass through to the partners and are included in the computation of the alternative minimum tax under I.R.C. § 55 at the individual partner level. I.R.C. §§ 703 and 704 address partnership computations and a partner's distributive share.

I.R.C. § 705 provides for the determination of the basis of a partner's interest. The general rule in subsection (a) provides that the adjusted basis of a partner's interest in a partnership shall, except as provided in subsection (b)¹, be the basis of such interest determined under section 722 (relating to contributions to a partnership) or section 742 (relating to transfers of partnership interests) -

(1) increased by the sum of his distributive share for the taxable year and prior taxable years of -

(A) taxable income of the partnership as determined under section 703(a),

(B) income of the partnership exempt from tax under this title, and

(C) the excess of the deductions for depletion over the basis of the property subject to depletion;

(2) decreased (but not below zero) by distributions by the partnership as provided in section 733 and by the sum of his distributive share for the taxable year and prior taxable years of -

(A) losses of the partnership, and

(B) expenditures of the partnership not deductible in computing its taxable income and not properly chargeable to capital account; and

(3) decreased (but not below zero) by the amount of the partner's deduction for depletion for any partnership oil and gas property to the extent such deduction does not exceed the proportionate share of the adjusted basis of such property allocated to such partner under section 613A(c) (7) (D).

The payment of regular income taxes by an individual, ie. a partner, under I.R.C. §§ 1 or 3 does not affect the determination of the basis of a partner's interest in a partnership under I.R.C. § 705.

Except as otherwise provided by statute or regulations, all code provisions that apply in determining the regular taxable income of a taxpayer also apply in determining the alternative minimum taxable income of the taxpayer.

¹ I.R.C. § 705(b) provides for an alternative rule where the Secretary shall prescribe by regulations the circumstances under which the adjusted basis of a partner's interest in a partnership may be determined by reference to his proportionate share of the adjusted basis of partnership property upon termination of the partnership. Such alternative rule is not applicable to the case at hand.


As such, the payment of Alternative Minimum Tax by an individual, ie. a partner, under I.R.C. § 55 does not affect the determination of the basis of a partner's interest in a partnership under I.R.C. § 705.

Based upon the foregoing, it is our office's position that the payment of Alternative Minimum Tax by an individual partner does not affect the partner's adjusted basis at the partnership level.

Our office has informally discussed the foregoing with subject matter specialists in the National Office. This memorandum will be sent to the National Office for a 10-day post review and our office will provide a written memorandum on such review. For any questions, please contact Theresa McQueeney, ID No. 11-01914, at (516) 688-1709.

DONALD SCHWARTZ
District Counsel

By:


LEWIS J. ABRAHAMS
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